IMPACTS OF A CHANGE IN THE METHOD OF PAYMENT: A DISCUSSION PAPER FOR THE AGRICULTURAL ADVISORY COUNCIL

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EXECUTIVE SUMMARY

The Agricultural Advisory Council, appointed by Manitoba's Minister of Agriculture in May 1989, was formed to initiate and guide research on a variety of agricultural and agri-food issues and has a mandate to advise and make recommendations to the Minister.

The first project undertaken by the Council and the subject of this paper involves an analysis of the impact of a potential change in the method of payment of the "Crow benefit" on Manitoba's economy. This discussion paper is the first of a series outlining the major findings of the research.

The recent Federal and Alberta government initiatives, the GATT concerns, and a desire to ensure Manitoba retains the optimal grain exporting system have caused the Agricultural Advisory Council to deem this study necessary to objectively analyze the implications of a potential change in the method of payment. From this, public input will be solicited to ensure Manitoba is in the best possible position to advance its interests in relation to what has been, and may in the future be, put forth by other provinces and the federal government. Also, the interests of farmers and others in the agricultural industry can best be served if all have the opportunity to receive information on this issue.

The research shows that the combined effect of inflation and increased grain volumes could increase the producer's share of WGTA rates to $29.08/tonne, up from the present average of $9.00/tonne, which is 323 percent of the existing rate, by the year 2000. Therefore, producers must recognize that they pay all cost increases in the grain transportation system. Thus, whether a pay the producer approach is implemented or the status quo situation is retained, the real costs of grain transportation will be increasingly borne by producers and will become more apparent.

The key to analyzing the implications of the existing WGTA rate structure versus a change in the method of payment involves the following:

1. Producers will likely pay all cost increases regardless of whether status quo is retained or a change is made.

2. Under a changed system, the Crow benefit payment could offset the initial higher freight rate grain producers would face from a change to pay the producer.

3. If, under a changed system, producers were able to make decisions resulting in less rapid cost increases, then grain producers, as well as others, could benefit.

From the individual producer's perspective a description of what a pay the producer approach would involve is best shown by an example:

Pay the Railway (Existing)			Pay The Producer
Export grain price		$100.00	$100.00
Freight Costs	21.00		21.00
Crow benefit (To R.R.)	14.70		
Producer Freight	6.30	6.30	____
Grain price		93.70	79.00
Crow benefit (to producers)		0	14.70
Net to Producer		$ 93.70	$ 93.70

Regional, sectoral, and individual differences will occur in the level of payment, relative to pay the producer freight increases caused by a change in the method of payment. This may result in a shortage or a surplus for individuals.

The studies conducted by a variety of groups indicate that production shifts in the grains sector will be relatively modest. Increases in cattle and hog production of 25 percent and 28 percent respectively could result from a change to pay the producer. A more substantial impact of such a change in the method of payment would occur due to the potential ending of interprovincial distortions in livestock feeding due to transportation related provincial subsidies, e.g., Alberta's Crow Benefit Offset Program. The research conducted indicates that the feeding of cattle in Manitoba could nearly double, followed by associated jobs in processing and economic benefits, if an inter-provincial "level playing field" existed between Manitoba and Alberta or Saskatchewan.

A key result of the research is the development of a relationship between changes in transportation costs and the amount by which farmgate grain prices may decline. Many previous studies have simplistically assumed a 1 to 1 relationship. However, this would not appear to be so. For some crops, the market reaction will, through several stages of direct and indirect responses, offset or "absorb" a portion of the freight rate increase. For example, it is estimated that farmgate prices for barley will decrease by approximately 50 percent of the increased freight rates. While this "market absorption" response varies dramatically by crop, it creates significant impacts.

Because WGTA rates are distance-related, rather than cost-related, the WGTA rate structure would not be fully compatible with a pay the producer approach. Under WGTA rates, farmers on main lines would be required to pay rates substantially higher than the railway's cost, and the railway would be unable to compete with trucks on an equal basis. This situation is untenable, as farmers in central and eastern Manitoba would wish to use the system with the lowest rates. Under WGTA rates, trucks would have lower rates than rail. Thus, farmers, railway companies, and others would press for changes from a WGTA rate structure to a commercial rate system.

A change to a pay the producer method of payment would create a new type of incentive system. For the first time, farmers would be paying the full cost of transportation and would, therefore, apply their management skill to reduce transportation costs and maximize their profits. It is also expected that these incentives would create pressure for many further changes in the regulatory and institutional structures which determine the tariffs and charges for grain handling and transportation.

Once commenced, the process of change would be extensive, with potentially unforeseen consequences to some industry participants. Given the co-ordination required for the system to work smoothly, and the capital intensive nature of both the grain handling and transportation systems, a phased and comprehensively planned process of change is required. This planning is necessary to minimize the negative economic impacts during the transition period. Without this planning significant inefficiencies could occur.

1.0 PROFILE OF THE AGRICULTURAL ADVISORY COUNCIL

The Agricultural Advisory Council, appointed by Manitoba's Minister of Agriculture in May 1989, was formed to initiate and guide research on a variety of agricultural and agri-food issues and has a mandate to advise and make recommendations to the Minister.

The interests of Manitoba business, agricultural producers, academia, and government are well represented on the Council, providing a perspective that is broad and cross-sectional, yet specific to the province. As such, the Council provides an opportunity for Manitoba farmers and the agricultural industry to influence agricultural policy.

The first project undertaken by the Council and the subject of this paper involves an analysis of the impact of a potential change in the method of payment of the "Crow benefit" on Manitoba's economy. This discussion paper is the first in a series outlining the major findings of the research.

2.0 BACKGROUND

On November 23, 1983, the Western Grain Transportation Act (WGTA) became law, replacing the statutory Crow Rates for moving grain. The new act, effective January 1, 1984, had been designed to gradually increase grain producers' share of freight costs, thereby removing its influence over time on the western livestock and processing industries.

Under the WGTA, the federal government committed $658.6 million per year to support the movement of export grain by rail. This amount represents the difference between the cost to the railways of transporting statutory crops in 1981-82 and the sum of what the railways had received for moving statutory crops under the Crow Rate. In addition, the government has made contributions to cover certain other costs, increasing its annual commitment, known as the "Crow benefit," to approximately $720 million.

It is commonly held that the Crow benefit represents an "historical entitlement" to western grain producers, but there has not been agreement as to how the benefit should be received. After considerable parliamentary debate leading to the passage of the WGTA, it was decided that the Crow benefit would be paid directly to the railways and that producers, in lieu of the direct benefit, would pay freight rates discounted in total by the amount of the benefit.

The WGTA has encouraged investment in the rail system, marking an improvement over the previous statutory provisions. It had become obvious that, without new investment, the rail system would be unable to transport the increased tonnage that western grain producers were capable of producing and selling internationally.

3.0 IMPETUS FOR THE STUDY

A number of recent political developments culminated in the project being undertaken. In view of these factors and the resulting significant implications, Manitoba producers and government clearly need to understand this complex issue.

3.1 Current Situation

The grain transportation and handling system has undergone dramatic change over the past 10-15 years and change will continue to occur. Over 50 percent of grain elevators in the west have been closed during this period. Of the 1,700 remaining elevators, 20 percent handle half the export grain. This has occurred as roads have improved - over 311,000 kilometres of all-weather roads have been built on the prairies during the past 60 years. However, much less change has occurred in the grain gathering rail lines, now totalling 27,400 kilometres - only 25 percent less than in the 1930's.

The WGTA Producer Rates, which represent only a portion of the total cost, have not provided farmers with the information necessary to evaluate the system. Some parties state that the below-cost rates have caused farmers to use transportation to a greater extent than would be the case otherwise, and also have resulted in farmgate grain prices being above levels that would otherwise be expected.

Some parties, in particular Alberta, feel the Act has not resolved certain inefficiencies in the grain handling system and disincentives to diversify on the prairies. By paying the benefit to the railways, rather than the producers, and having freight rates that do not reflect real costs, these parties claim, the WGTA has dampened the incentive for farmers to seek greater efficiency in the grain handling and transportation system and has disadvantaged livestock production and secondary processing on the prairies.

Among its major competitors, Canada has the greatest distance from grain production areas to seaports. Therefore, the grain handling and transportation system warrants close attention, as it forms a significant portion of the total cost of export grain placed in a marketable position at a seaport. Also, the dependence on exports will continue in the future and it is critical to ensure that the best possible grain handling and transportation systems is maintained.

As farmers pay all cost increases in the grain handling and transportation system, the Agricultural Advisory Council deemed a study warranted to review how farmers might be able to reduce cost increases they face in the future.

3.2 Federal Government Policy Review

The federal Agriculture Minister has commissioned an overall review of virtually every Agriculture Canada program and policy. The federal government is reportedly interested in obtaining a greater return on its investment in agriculture

by making the sector more viable through diversification and value-added processing.

One of the major issues that will likely result from these diversification discussions is the future of the WGTA. It is a widely held view by Agriculture Canada that payment of the Crow benefit obstructs value-added processing.

To prepare for such negotiations and be in the best position to represent Manitoba's interests, this study was commissioned.

3.3 Alberta's Policy Initiative

In 1986, the governments of Alberta and British Columbia formed a task force to review the situation, develop alternative payment schemes, and assess the impacts of a change in the method of payment of the Crow benefit. The task force has proposed that B.C. and Alberta's shares of the Crow benefit be paid directly to B.C. and Alberta producers on an experimental basis, proceeding independently of other provinces. In addition, to avoid diluting B.C. and Alberta producer payments, the proposal recommended that the Alberta government contribute an additional $100 million.

Manitoba's reaction has been that such a program would attract secondary processing, diversification, and the livestock sector to Alberta. Manitoba could not afford the approximately $30 million necessary to compete with such a program - provincial farm spending is only $80 million in total.

The Agricultural Advisory Council is unanimously opposed to a B.C./Alberta pilot project with this level of provincial cash injection, even on a trial basis.

3.4 International Trade Negotiations

Ongoing GATT negotiations have identified that some countries perceive the WGTA to be an export subsidy. Recent submissions by the U.S. on proposals for comprehensive long term agricultural reform have adverse implications for the WGTA. The GATT negotiations hold potential to create pressures for a new approach to dealing with the Crow benefit.

The factors described above have caused the Agricultural Advisory Council to deem this study necessary to objectively analyze the implications of a potential change in the method of payment. Public input is now being solicited to ensure Manitoba is in the best possible position in advancing Manitoba's interests in relation to what has been, and may in the future be, put forth by other provinces and the federal government. Also, the interests of farmers and others in the agricultural industry can best be served if all have the opportunity to receive information on this issue

4.0 OBJECTIVES OF THE STUDY

The overall objectives of the project are to seek information and gain an understanding of the issues and implications of a possible change in the method of payment. From this process, the framework will have been established to provide information to all interested parties to assist in analyzing what is best for the Manitoba farm community and the economy as a whole. The purpose of the study was not to prescribe recommendations related to this issue.

This paper is the first in a series summarizing and communicating the results of the research conducted during the study. The complexity of the issue and the variety of inter-relationships between commodities and sectors make it necessary to present the information in several discussion papers.

5.0 COST TO THE FARMER OF MAINTAINING THE STATUS QUO

One of the main reasons for undertaking the study was the concern raised by certain provisions in the Act over how the WGTA rates will escalate in the future. This section of this paper provides information on the dramatic cost increase producers can expect in the future under the present system. These increases occur in rail freight costs and overall systems costs.

5.1 Rail Freight Costs

Currently, WGTA total rates are shared by the federal government and the producer. Table 5.1-1 compares the producers'share to the WGTA total rates since the inception of the Act, for the distance scale interval of 901-925 miles, the average distance for the prairies over which grain is transported by rail. Basically, the WGTA total rates cover the cost of the entire grain transportation system provided by the railways.

Table 5.1-1 Average WGTA Rates and Producer's Share

Crop Year	WGTA Total Rate ($/tonne)	Producer's Rate ($/tonne)	Producer's Share (%)
Pre-1984[1]		4.85	
1984[2]	27.60	5.72	20.7
1984[3]	27.40	7.70	28.1
1985/86	29.13	6.00	20.6
1986/87	30.94	5.97	19.3
1987/88	30.46	6.34	20.8
1988/89	30.26	7.27	24.0
1989/90	30.31	9.00	29.7

1 Crowsnest Pass Rate
2 Jan. 1, 1984.
3 Aug. 1, 1984.

The federal government contribution is essentially fixed in the amount of the $720 million Crow benefit and, given the present inflationary trends, is likely to remain so. Conversely, the amount paid by producers will increase, and depends on two main factors. First, the Act specifies that the producers pay the full amount of the annual cost increase in grain rail transportation due to inflation up to 6 percent. Any costs above 6 percent are to be paid by the Federal Treasury. Second, the Act stipulates that the producer also pays the full incremental cost of any volume increases.

Freight rate increases are subject to a "safety net" provision. For 1988 and later years, the WGTA has required that average statutory freight rates paid by producers is not to exceed 10 percent of the average selling price for grains at ports of export.

5.1.1 Inflationary Increases

Since the Act was passed, the railway cost inflation rate has only once exceeded 6 percent. The inflationary increase related to the cost of moving grain has been relatively small compared to that of the general economy. The national average annual rate of inflation over the past ten years has been 7.8 percent, while the rate of increase in rail grain costs has been approximately 1.9 percent. Even in this situation, the producer's share of the rate has increased from $5.72/tonne when the WGTA was implemented in January 1984, to the present $9.00/tonne. This is a 57 percent increase since 1984.

The current average WGTA total rate is $30.31/tonne. If inflation were sustained at a rate of between 1.9 and 5.0 percent, by the crop year 1999/2000, the average rate would increase to between $36.59 and $49.37. The producer's share would rise from $9.00 to between $15.28 and $28.06/tonne, assuming annual inflation rates of 1.9 and 5.0 respectively, and assuming the level of grain prices were not to limit the freight rate increase. This represents an increase of between 70 and

212 percent and illustrates only the inflationary effect. This phenomenon is illustrated in Appendix 1.

5.1.2 Volume Increase

Producer freight rates could rise due to inflationary cost increases, and from increased volumes of export grain. There are conflicting views in regard to the amount of grain that will be shipped for export in the future. However, if the Canadian Wheat Board's view is accepted, exports can be expected to increase to between 34.0 and 35.5 million tonnes by the year 2000. Therefore, the producer would be responsible for paying the additional costs associated with increased volumes, while the government contribution would remain fixed.

Table 5.1-2 shows the combined effect of inflation and increased grain volumes. This analysis illustrates that the producer's share could rise from 29.7 percent of the WGTA total rate to between 42.1 and 58.9 percent, depending on the assumptions that are made for inflation and grain volume. This combined effect could increase the producer's share to $29.08 per tonne, which is 323 percent of the existing rate.

Table 5.1-2 Effect of Increased Grain Volume on Producer's WGTA Rate for the Year 2000

Volume of Shipments (million tonnes)	$36.59[1]	$49.37[2]
	Total Freight Rate per Tonne	
	Producer's Share of Freight Rate (%)	
34.0	42.1%	57.1%
35.5	44.6%	58.9%

1. WGTA Total Rate, assuming 1.9 percent inflation.
2. WGTA Total Rate, assuming 5.0 percent inflation.

5.2 System Costs

Producers currently pay approximately $10.10/tonne for country elevation and handling. This is larger than the present $9.00/tonne average for the producer's share of the WGTA rates. With industry estimates of inflationary cost increases of approximately 5 percent per year for country elevation, the future costs to producers for handling can be expected to increase dramatically.

Thus, under a scenario of moderate inflation, increased grain volumes, and normal grain prices, grain freight rates and handling costs will escalate. Producer freight rates would also increase under a pay the producer approach where producers would pay the entire freight rate rather than just a portion. But, under the current WGTA legislation, the freight rates would include the cost of maintaining the existing grain transportation system.

Therefore, producers must recognize that they pay all cost increases in the grain transportation system. Thus, whether a pay the producer approach is implemented or the status quo situation is retained, the real costs of grain transportation will be increasingly borne by producers and will become more apparent.

The key to analyzing the implications of the existing WGTA rate structure versus a change in the method of payment involve the following factors:

1. Producers will likely pay all cost increases, regardless of whether status quo is retained or a change is made.

2. Under a changed system, the Crow benefit payment could offset the higher freight rate grain producers would face from a change to pay the producer.

3. If, under a changed system, producers were able to make decisions resulting in less rapid cost increases, then grain producers, as well as others, could benefit.

6.0 "PAY THE PRODUCER" FROM THE INDIVIDUAL PERSPECTIVE

A change in the method of payment from paying the railways to paying the producer would place additional money in the hands of producers. The Crow benefit payment to the producer on a 1000 acre commercial farm could be $15,000 per year or more. Producers would then be able to determine how best to spend those financial resources: to pay the additional rail freight rates; to use a substitute mode of transportation, e.g. trucking; to shift production to other crops or livestock; or to market crops to new markets with reduced freight costs.

An example representing what an individual farmer would see in such a change is shown below in table 6.0-1.

Table 6.0-1

Pay the Railway (Existing)			Pay The Producer
Export grain price		$100.00	$100.00
Freight Costs	21.00		21.00
Crow benefit (To R.R.)	14.70		
Producer Freight	6.30	6.30	____
Grain price		93.70	79.00
Crow benefit (to producers)		0	14.70
Net to Producer		$ 93.70	$ 93.70

As seen in this simplistic example, the Crow benefit payment exactly offsets the increased freight charges and the farmer has the same cash in the pocket either way. However, it is quite possible that if a pay the producer approach was introduced, the payment would not exactly match for each farmer, even if on average it exactly matched the increased freight rates. There will be regional, sectoral, and individual differences in the level of payment relative to freight increases due to a change in the method of payment, creating a shortage or surplus in the payment to individuals.

Only in-depth analysis of a wide variety of alternative payment mechanisms, each having a variety of characteristics (e.g. based on grain sales, arable acres, etc.) and implications, can create an understanding of the implications for various groups. A later discussion paper will cover this topic.

7.0 IMPACT ON FARMER'S DECISION MAKING

Surveys indicate that many producers are not familiar with the level of transportation rates or tariffs for country elevation. This finding suggests that producers may not have the information needed to make decisions involving the costs of the grain handling and

transportation system. The present WGTA method of payment contributes to this obscuring of the full costs.

With a change in the method of payment to a pay the producer approach, Manitoba farmers would have the opportunity to make production, marketing, and transportation decisions based on their own business judgement. This is diagrammatically shown in in Appendix 2. As freight rates paid by farmers increase, farmgate grain prices would decline. This decline would be offset by the Crow benefit payment. Assuming that producers receive compensation equal to the amount of the increased transportation costs, farmers could then benefit by adjusting production, marketing and transportation decisions.

Of course, a change in the method of payment will impact individual farmers differently, and each will respond differently to such a change. For example, alternative production opportunities may be limited by land that is suitable only for the production of a particular crop, or commodities that require specialized equipment or expertise. The greater the availability of production alternatives, the easier it is for farmers to respond to changes in freight rate increases.

Increased transport charges would be levied on a per tonne basis, regardless of the value of the crop. As such, economic incentives would exist for farmers to shift crop production into a mix that maximizes returns. This would include a relatively greater proportion of crops which face the smallest freight increase. Therefore, if the Crow benefit payment were to offset the increased costs of higher freight rates, producers could employ their management skills to secure a net gain.

The studies conducted by a variety of groups indicate that production shifts in the grains sector will be relatively modest. A second, more significant shift would also likely occur as a result of the lower priced feedgrains in Manitoba. As feedgrain prices fall, livestock production, which uses these commodities as an input, can be expected to expand. Compared to the inter-crop production shifts, this change in livestock output would be

more significant, but would occur more slowly, over a longer time period. Increases in cattle and hog production of 25 percent and 28 percent respectively could result from a change to pay the producer. A more substantial impact of such a change in the method of payment would occur if interprovincial distortions in livestock feeding caused by transportation related provincial subsidies (e.g. Alberta's Crow Benefit Offset Program) were removed. The research conducted indicates that the feeding of cattle in Manitoba could nearly double, followed by associated increases in jobs in processing and economic benefits, if an inter-provincial "level playing field" existed between Manitoba and Alberta or Saskatchewan.

A key result of the research is the development of a relationship between changes in transportation costs and the amount by which farmgate grain prices may decline. Many previous studies have simplistically assumed a 1 to 1 relationship. However, this would not appear to be so. For some crops, the market reaction will, through several stages of direct and indirect responses, offset or "absorb" a portion of the freight rate increase. For example, it is estimated that farmgate prices for barley will decrease by approximately 50 percent of the increased freight rates. While this "market absorption" response varies dramatically by crop, it creates significant impacts.

8.0 IMPACT ON THE GRAIN HANDLING AND TRANSPORTATION SYSTEM AND PROCESSING SECTOR

Currently, producers are locked into a grain transportation system served only by the railways and characterized by administered freight rates, regardless of cost variations within the system. The current system obscures the real costs of grain transportation, providing farmers with little opportunity to manage their own transportation costs. If the full cost of grain transportation were made apparent to the farmers, they would be motivated to search for the most cost-effective means to market grain. Acting in their own self-interests, farmers would essentially be choosing an efficient grain handling and transportation system. This would contribute to producers' long run survival in a

competitive international marketplace through utilizing the optimal grain system in terms of services vs. costs.

8.1 Competitive or Variable Rates

Under WGTA, railway costs are determined on a system-wide basis. All grain producers share the cost of this system. WGTA rates are average rates representing the total cost of the whole rail system, including both high cost lines and low cost main lines. These rates reflect only the distance to the port of export, not real operating costs. Thus, under WGTA rates, producers on main lines would pay rates higher (perhaps by as much as 30 percent) than the real costs. As such, main line commercial rates, if allowed, would be lower than the corresponding WGTA total rates, while branch line rates would be higher. The possibility of competitively determined commercial rail rates rather than WGTA rail rates is explained in the next section.

Freight rates on branch lines would only increase to the level at which commercial trucking would become a viable alternative. Where it is viable, competitive market forces would intervene, tempering the amount of the freight rate increase. Consumers are typically the beneficiaries of increased market competition, and this case would be no different. Farmers, as shippers of grain, are consumers of transport services and can expect to pay lower freight costs as a result of the increased modal competition. This intermodal competition between rail and truck would apply most extensively in eastern and central Manitoba.

In the view of the trucking industry, opportunities exist for intermodal competition in grain handling and a reduction in grain transportation costs. In addition, the quality of service that trucking offers would provide additional flexibility to farmers shipping grain.

8.2 Future Structure of the Grain Transportation and Handling System

Because WGTA rates are distance-related, rather than cost-related, the WGTA rate structure would not be fully compatible with a pay the producer approach. Under WGTA rates, the farmers on main lines would be required to pay rates substantially higher than the railway's cost and the railway would be unable to compete with trucks on an equal basis. This situation is untenable, as farmers in central and eastern Manitoba would wish to use the system with the lowest rates. Under WGTA rates, trucks would have lower rates than rail. Thus, farmers, railway companies, and others would press for changes from a WGTA rate structure to a commercial rate system.

Under a commercial rate system, it is expected farmers would find a number of branch lines and related elevator points in Manitoba to be unattractive and would shift to a lower cost point. If rail freight rates increased to reflect real operating costs, farmers located on many branch lines would find trucking to be a more viable alternative. It follows that, if the truck and rail industries were expected to compete on price and service, the only way the railways would be able to do so, is if they were allowed to decrease rates on high volume lines. Trucks would serve the uneconomical lines.

The view held by many of those close to the issue is that, if the payment were made to the producer, it would lead to pressure for the Western Grains Transportation Act to be revised or eliminated. If not, potential exists for major transport anomalies to occur because railway companies would then be at a competitive disadvantage relative to the trucking industry on a number of high-volume lines.

8.3 Processing Sector

The most significant impact on the Manitoba processing sector would occur in the livestock slaughter/processing and the oilseed crushing sectors. With potentially significant increases in livestock feeding, the livestock slaughtering and processing sector could rebound from the economic decline suffered in the recent past.

9.0 ALTERNATIVE CROW BENEFIT PAYMENTS

Throughout the Crow Rate debate in the early 1980's, the most contentious issue was whether or not grain producers should pay higher freight rates. However, by the spring of 1982, it was possible to state that a general consensus existed that the railways lost money and the Crow rate should be changed. The debate then shifted to who should receive the federal government subsidy - the railways or the grain producers. In addition to the question of railways vs. producer, there is also the matter of how to deliver the Crow benefit to the producer, if that option were selected.

There are many alternative mechanisms for pay the producer methods of payment. The key characteristics identified which would form pay the producer alternatives are as follows:

- Annuity vs. bond vs. program payment
- Length of payment period
- Size of payment
- Transferability
- Transition period
- Dilution compensation
- Delivery mechanism
- Tax status

- Base period for calculation of payment
  .. future
  .. historic
- Receiver of the payment
- Basis for calculation
  .. rail shipments
  .. production
  .. arable acres
  .. etc.

Each characteristic has a number of alternatives, each with variations in the impacts of the payment of the Crow benefit on the producer. A number of fundamental issues were identified, including:

- equitability
  .. in terms of status quo - winners vs. losers
  .. between groups, e.g. livestock vs. grain

- resource neutrality
  .. diversification and efficiency

- dilution effects.

10.0 EXTENSIVE IMPLICATIONS

A change to a pay the producer method of payment would create a new type of incentive system. While the producer would receive a Crow benefit payment, for the first time, farmers would be paying the full cost of transportation and would, therefore, apply their management skill to reduce transportation costs and maximize their profits. Thus, the source of change would no longer be regulatory agencies, railroads or political

organizations, but rather would become the large number of farmers, each motivated to create further changes which would reduce their transportation costs.

This would lead to pressures in Manitoba from those farmers delivering to main line rail locations wishing to utilize commercial trucking or obtain commercial rates. It is also expected that pressures from these incentives would occur for many further changes in the regulatory and institutional structures which determine the tariffs and charges for grain handling and transportation.

The Canadian Wheat Board (CWB) procedures for pooling of grains have been discussed several years ago, with regard to revisions to the locations for pricing, i.e. FOB Vancouver and Thunder Bay, being changed. While the previous suggestions for change would have negatively impacted Manitoba and were deferred, a change in the method of payment may have indirect implications, creating renewed pressures for some type of amendment to CWB pooling procedures.

Research is being completed on other aspects of the potential impacts of a change to a pay the producer approach, including implications for rural communities.

Once commenced, the process of change would be extensive, with potentially unforeseen consequences to some industry participants. Given the co-ordination required for the system to work smoothly and the capital intensive nature of both the grain handling and transportation systems, a phased and comprehensively planned process of change is required. Without these conditions, chaos and inefficiency could occur during the transition period.

11.0 COMPLEXITY

To understand this complex area, it is necessary to recognize that the Crow benefit payment is only one of two factors creating change. The other is the increased freight rates which the farmers would then have to pay. Depending upon the characteristics of

the payment mechanism, these two factors may be largely separate and unassociated or they could combine under some payment mechanisms to exert forces for change. The attached Appendix 3 displays this set of forces diagrammatically.

In addition, the complexity of the analysis of the method of payment is compounded by:

- a number of sectors (production, transportation, processing, etc.) and commodities are involved and they are interactive such that a change in one creates impacts on others,

- the direct impacts of a change in the method of payment are only a part of the total impact; a large number of secondary and less direct effects also occur, with very significant potential impact,

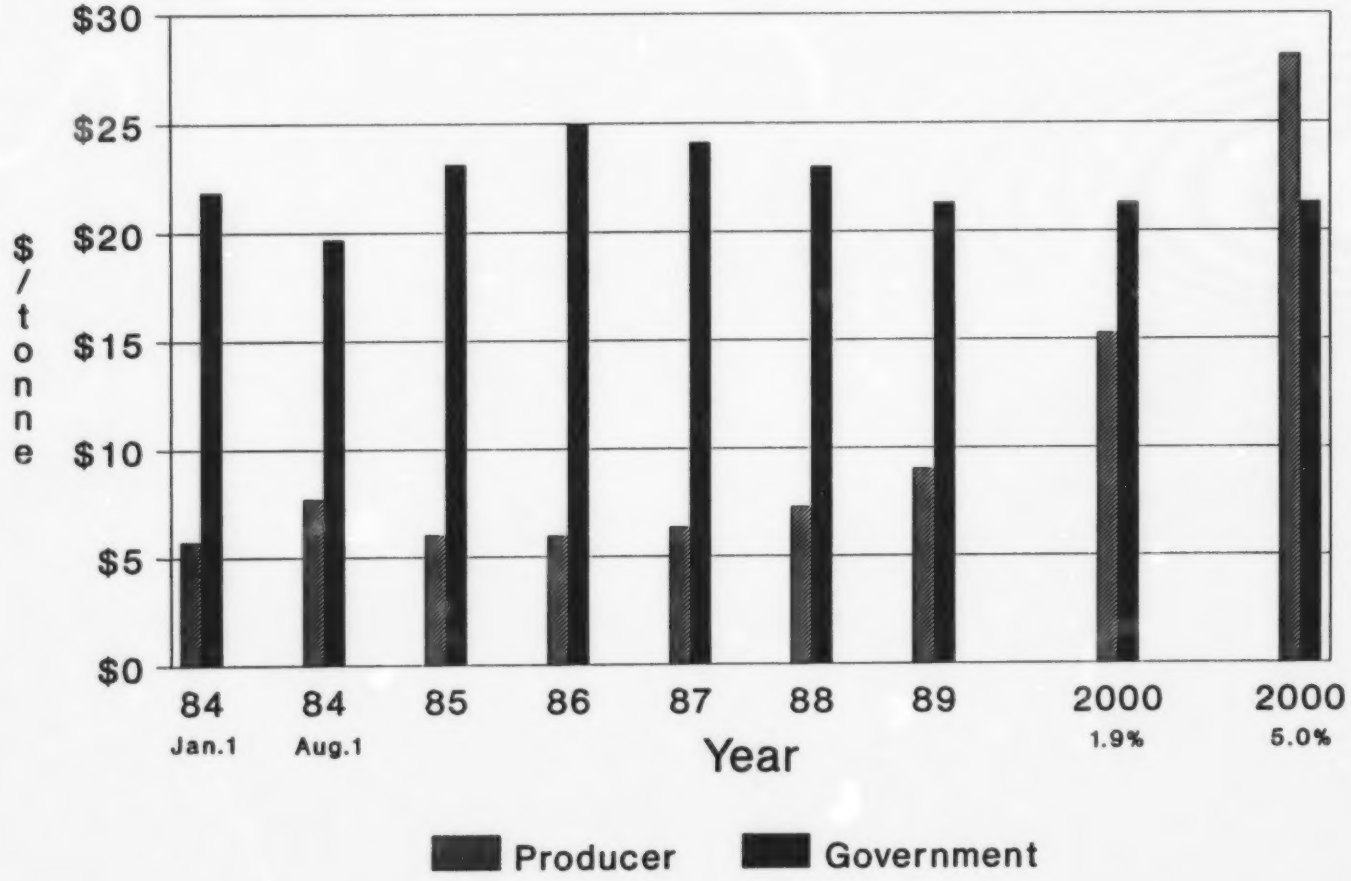
- the process of change creates both opportunities and challenges. Therefore, the responses of people and companies will dictate the final impacts of change.

12.0 FURTHER INFORMATION

This discussion paper is the first in a series. Further details of the research will be reported in the future, covering areas included in a brief preliminary manner in this paper, and covering other areas related to this topic.

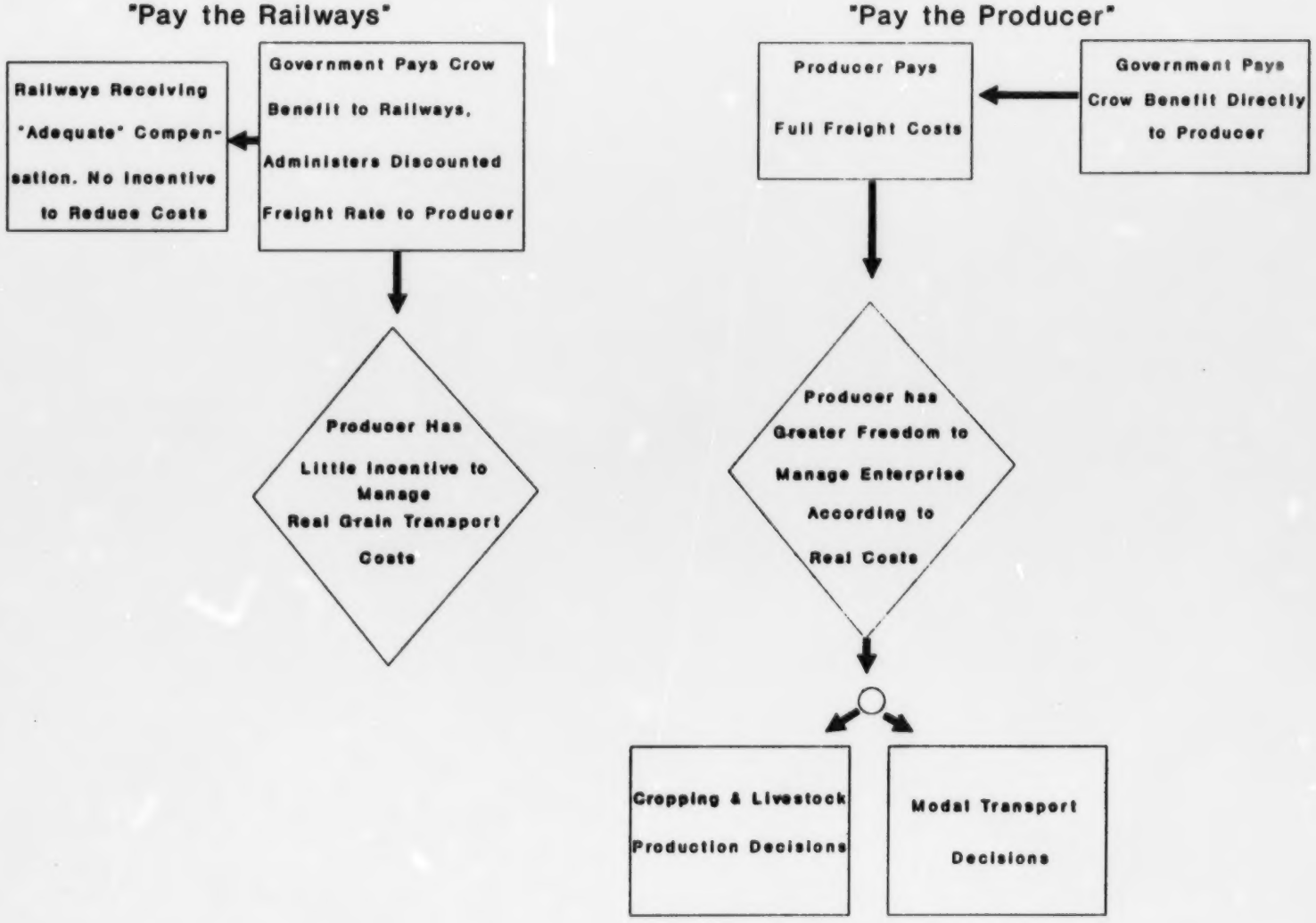
APPENDIX 1

Inflationary Effects on
Producer's Share, 1984-2000



APPENDIX 2

Method of Payment and Producers' Decisions


"Pay the Railways"
Railways Receiving "Adequate" Compensation. No Incentive to Reduce Costs
Government Pays Crow Benefit to Railways, Administers Discounted Freight Rate to Producer
Producer Has Little Incentive to Manage Real Grain Transport Costs
"Pay the Producer"
Producer Pays Full Freight Costs
Government Pays Crow Benefit Directly to Producer
Producer has Greater Freedom to Manage Enterprise According to Real Costs
Cropping & Livestock Production Decisions
Modal Transport Decisions

APPENDIX 3

TWO FACTORS CREATING CHANGE: FREIGHT RATE AND THE PAYMENT